City of San Diego

CARL DEMAIO

CITY COUNCILMEMBER –DISTRICT 5

MEMORANDUM

DATE: February 17, 2009

TO: Councilmember Tony Young

CC: Mayor and City Council
Independent Budget Analyst

FROM: Councilmember Carl DeMaio Carl DeMaio

RE: Fringe Benefit Costs

Enclosed is analysis I requested from the California Foundation for Fiscal Responsibility on fringe benefit costs. At the first meeting of the Budget Committee, I released a memorandum from the City's Office of Financial Management that calculated the city's fringe benefit rate at 61.28% of budgeted salaries.

The enclosed analysis sheds additional light on and provides key questions for the Council and the public to ask about the nature and cost of these benefits. There are different methods for compiling and comparing fringe benefit costs—and the city labor unions have disputed portions of the city's cost estimate.

Using the city calculation, the analysis shows the city's costs are higher than the national averages for state and local government. The analysis also argues that the City's calculation omits key fringe benefits costs. Including these would result in fringe benefit costs substantially higher than the national averages.

I have requested that the Independent Budget Analyst review the recommendations contained in the CFFR report and assist us in getting all stakeholders to adopt a common definition and calculation methodology.

As I requested when I released the city's memo, I'd like to see the issue of fringe benefit costs docketed and discussed in greater detail at the Budget Committee. Examining this issue would allow the Council and the public to better understand the exact level of benefits provided to city workers – and the net cost to taxpayers. I look forward to working with you on this important issue.

MEMORANDUM

TO: Councilmember Carl DeMaio
City of San Diego

FROM: Marcia Fritz
Vice President

DATE: February 13, 2009

RE: Fringe Benefit Analysis in the City of San Diego

Thank you for the opportunity to review and comment on fringe benefit rate figures you obtained from the City of San Diego's Office of Financial Management. I want to applaud your leadership in raising the issue of the cost of employee fringe benefits as part of an overall solution to San Diego's current budget deficit and long-term financial problems.

Scope of Analysis

I understand that you have asked your City Council to conduct a hearing on fringe benefit costs. In preparation for that hearing you requested that we prepare an analysis that would:

- examine the component elements and calculation methodology of the city's rate to determine whether it included appropriate items,
- suggest ways to compare the city's fringe benefits,
- offer any readily available analysis on how the city's fringe benefits compare to appropriate benchmarks, and
- offer ideas for additional analysis and reform of city labor costs.

To facilitate a more robust analysis and comparison of your city's fringe benefits and overall compensation, we recommend among other things that your scope of analysis on this topic be expanded to include the following:

- Request that either the Office of Financial Management or your Independent Budget Analyst respond to the methodological questions raised in this report,
- Review various national benchmarks on fringe benefits, but examine employee compensation and benefits from the most useful measurement: your city's ability to recruit and retain quality employees, and
- Seek out data and comparisons in your local labor market on a benefit-specific basis and a job-function-specific basis.

Summary of Analysis

While there are a number of different ways to calculate fringe benefits – and comparing fringe benefit rates is difficult for reasons outlined in our analysis – we make the following observations in this report:

- **City Calculation**: The city calculation of fringe benefits includes appropriate items, including the unfunded liability for the pension. However, we raise concerns that the city calculation has omitted a number of items that are traditionally considered fringe benefits including the cost for compensated abenses (or "annual leave"), overtime, and other allowances for city workers as stipulated in the city labor contracts.

- **Opportunity for Benefits Reform:** With the economic slowdown, employers are trimming benefits packages significantly. With unemployment on the rise, the city faces an excellent labor market and will likely have the ability to reform its benefits without an impact on recruitment and retention.

- **National Comparisons**: Due to complexities and differences in the calculation of fringe benefits, national comparisons of overall fringe rates are of limited usefulness. Bureau of Labor Statistics data uses a different calculation methodology than the one used by the City. When adjusting for differences, the City fringe benefit rate is still higher. Revised treatment of the omissions identified above will likely result in an even higher rate for the City compared to BLS averages.

- **Best Benchmark Approach**: Instead of using overall fringe rate comparisons, it is recommended that the City adopt a line-item focus to examining fringe benefits. The two largest line items are retirement and health.

- **Retirement Benefits**: The City of San Diego offers current city workers a retirement package on the highest end of benefits – and has a higher cost as percentage of compensation than private industry and state and other local governments.

- **Health Benefits**: The City of San Diego pays a higher percentage of the cost of health insurance than the national coverage percentage for state and local government.

Putting Government Fringe Benefits Into Context

In analyzing city employee pay and benefits, it is important to examine compensation and options for cost savings both by challenging myths and assumptions – and by placing all pay and benefits in the context of the conditions in your local labor market.

Challenging Myths and Assumptions

A common myth exists that local government employees are receiving less compensation than the private sector. Substantial evidence exists to refute this myth. A study by the Employee Benefits Research Institute concluded the following:

> *As of September of 2007, **overall total compensation costs were 51.4 percent higher** among state and local government employers ($39.50 per hour worked) than among private-sector employers ($26.09 per hour worked). Total compensation costs consist of two major categories: wages and salaries and employee benefits. For both of these categories, state and local government employers' costs were higher than those of private-sector employers: 42.6 percent higher for wages and salaries and **72.8 percent higher for employee benefits**.*
>
> *The differences in compensation costs between public-sector and private-sector employers are driven by the differing mix of job functions, work force composition, and concentrations of workers. The composition of the benefit package is another major factor in explaining the difference in compensation costs. Benefit participation rates are higher for state and local government employees and the costs of providing these benefits are higher.*[1]

Due to the disparity between perceptions and reality on this issue, it is important to challenge assumptions when discussing government employee compensation. It is for this reason that a focus on **actual** labor costs – both in generating data internally for decision making but also for public dissemination – is extremely important.

Your focus on “fringe labor costs” is equally important. The use of “fringe benefits” to spike government employee compensation is no secret in the ranks of government employees – as the advice provided on a government job recruitment website by the Local Government Institute illustrates.

[1] McDonnell, Kenneth J.,Benefit Cost Comparisons Between State and Local Governments and Private-Sector `Employers(June 2008). EBRI Notes, Vol. 29, No. 6, June 2008.

Working the System

Advice for current and prospective local government job-seekers from **Govtjob.Net** -- sponsored by the **Local Government Institute (LGI)**.

“Bargain for as many fringe benefits as possible before being hired. Fringe benefits are an important consideration in any Local government manager's total compensation package. They often represent 25-45% of a manager's salary.”

“Fringe benefits not only provide you with additional security, but they also serve to offset expenditures that would otherwise come out of your disposable income. Sometimes fringe benefits are better than the equivalent salary increase because the fringe benefits may frequently be treated as non-taxable income, and often more politically negotiable.”

Source: http://www.govtjob.net/NegotiateEmp.htm

Another common myth is that, because of the stress and hazards of their work, public safety workers have shorter lifespans than other workers so the cost of they deserve rich pensions. In its demographic experience study in May, 2004, CalPERS found no differences in post-retirement mortality rates by job-type, but did predict longer post-retirement life expectancy for male retirees and beneficiaries.

Decision-makers and the public are becoming increasingly aware of and concerned by the cost of city employee pensions and retiree health care. This awareness and concern, however, is driven by the explosive growth in the costs for those two benefits.

By raising questions on the cost of the City of San Diego’s <u>total</u> fringe benefits, you are correctly expanding the discussion of city employee compensation to cover the true net costs of labor to the city taxpayers.

Conditions in Local Labor Market

Partially driven by the myth above, and partially driven by pressures from municipal labor unions, many government employers have lost sight of the overall goal of employee compensation packages.

Put simply, an employer’s salary and benefits should be set at a level that allow the employer to win the war for talent in its local pool of labor.

The best indicator of whether the City of San Diego on the appropriateness of its pay and benefits package is the important metric of recruitment and retention – particularly on a job function level.

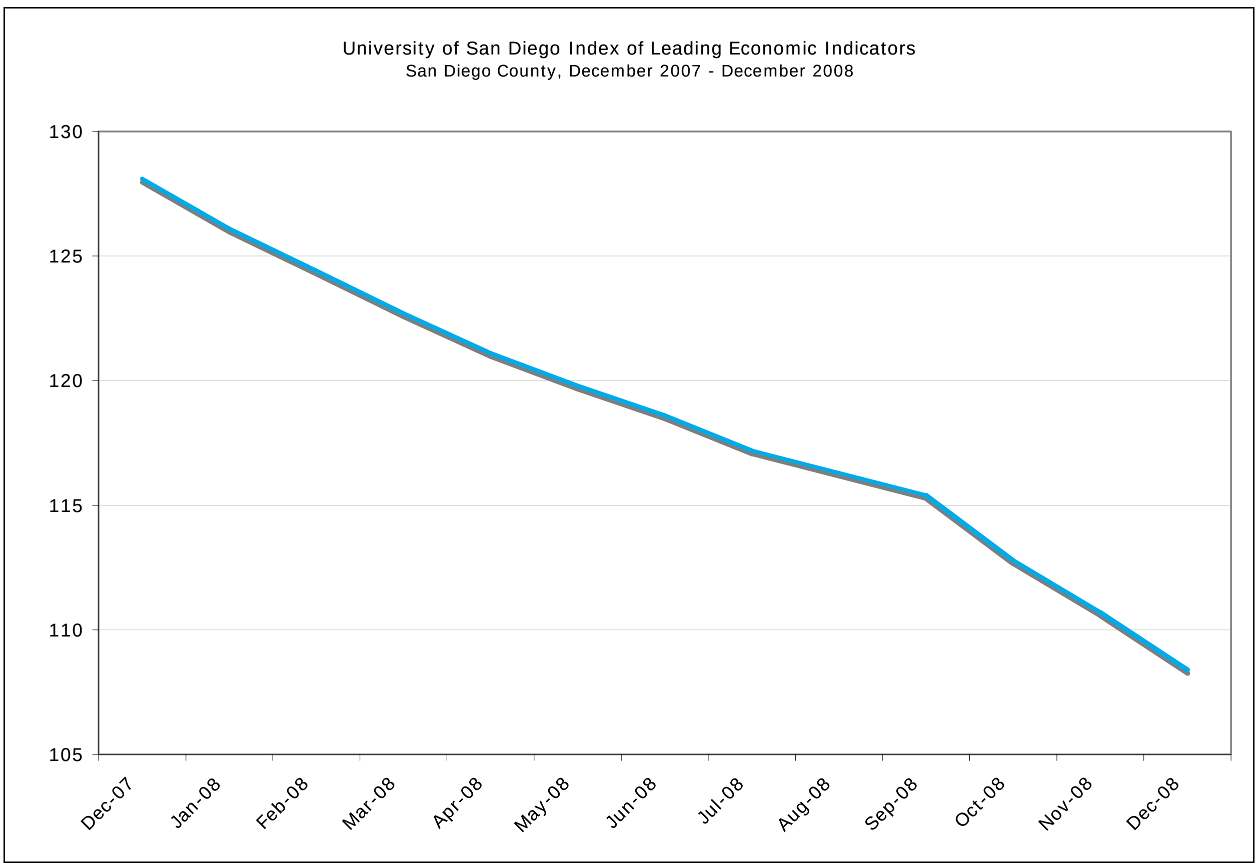
For example, when the City was having difficulty recruiting police officers, it commissioned a study to compare pay and benefits with other police departments. That study could have examined related job functions such as the military. It also could have explored ways to increase its pool of qualified applicants through policy changes outside pay and benefits.

Another contextual issue to consider in discussing city employee pay and benefits are the current conditions in the local economy and labor market.

While a full analysis of the local San Diego labor market is beyond the scope of this report, ample evidence exists to suggest the city is operating in a highly favorable labor market for an employer.

According to the most recent iteration of the monthly University of San Diego (USD) regional economic index, which tracks building permits, initial unemployment insurance claims, San Diego stock prices, consumer confidence, help wanted advertising and the national economy:

> *The outlook remains unchanged from recent months. The local economy is expected to be weak for at least the first half of 2009, with job losses in particular expected to mount. While job losses had previously been confined to real estate-related areas (construction, credit, real estate), the damage is now spreading into other sectors of the local economy. Retailing has been heavily impacted, with a weak Christmas buying season causing retail employment to fall by 8,500 jobs in December compared to the same month a year ago. The numbers are expected to worsen with the post-holiday closing of stores such as Mervyn's, Circuit City, and Linens 'n Things.*



Using market-based principles related to recruitment and retention will allow the City to accurately gauge the sufficiency of its employee compensation. A government job is a highly attractive one – particularly in this economic climate. The City of San Diego's compensation should reflect economic realities.

The recent economic downturn possibly provides the city with an opportunity to reduce its pay and benefits without compromising its competitiveness in recruitment and retention.

Review of City Fringe Rate Calculation

"Fringe labor costs" or "fringe benefits" can be defined—and calculated—in a number of ways.

The City listed the following line items in its list of fringe benefits:

Fringe Title	FY 2009 Budget	% Fringe
ARC for Retirement	$161,705,323	25.92%
SPSP	$23,952,721	3.84%
Retirement Offset Contribution	$19,505,202	3.13%
Employee Offset Savings	$19,738,384	3.16%
Workers Compensation Insurance	$25,999,363	4.17%
Flexible Benefits	$59,338,459	9.51%
Risk Management Administration	$6,599,088	1.06%
Long Term Disability	$5,333,924	0.86%
Unemployment Insurance	$1,081,307	0.17%
FICA/MEDICARE	$8,587,377	1.38%
Retiree Health/OPEB	$50,001,169	8.01%
Unused Sick Leave	$429,000	0.07%
Total	**$382,271,317**	**61.28%**
Budgeted Salaries	$623,849,572	

The City's calculation includes acceptable items in its list of fringe benefits. Moreover, the method used by the City of San Diego to calculate fringe benefits as a percentage of salaries is "common in employee benefits parlance."[2]

At one recent budget committee meeting a representative of a labor union asserted that inclusion of the unfunded liability was inappropriate and inflated the city's overall fringe rate. Pursuant to an inquiry with the Bureau of Labor Statistics, the City is correct to include the payments it is making for the unfunded pension liability into its calculation of fringe benefits. Furthermore, the unfunded liability was initially created by plan amendments that provided retroactive benefit increases with the expectation that the City would realize economic benefits in future periods.

It is important to note that more than three-quarters of the city's pension liability stems from factors outside of underfunding the system. Specifically the 2004 "Final

Common Elements in Fringe Benefits

Paid Leave
Including vacation days, sick days, paid holidays, and other paid time off

Retirement and Savings
Including employer contributions on behalf of employees for defined benefit and defined contribution plans (also Social Security if applicable)

Health Insurance
Including health and dental insurance – for current employees and retirees

Other Insurance
Including short and long term disability, federal and state unemployment insurance, workers compensation, state temporary disability insurance

Allowances
Including training allowances, membership fees for professional associations, vehicle allowance, uniform allowances, Presidential Leave, take-home cars, dependent care, wellness programs, etc.

Supplemental Pay
Including overtime.

[2] Chen, Yung-Ping. "The growth of fringe benefits: implications for social security." *Monthly Labor Review*: November 1981.

Report" of the Pension Reform Committee listed "benefit improvements" as the largest contributor to the "under-funded problem." Moreover, actuarial assessments made since the PRC report have only served to reinforce the fact that the vast majority of the liability stems from factors other than underpayment of the ARC in previous fiscal years. Regardless of the source of the liability, the cost of any liability should be included in the fringe benefit rate.

The City is correct to include the payments it is making for the unfunded pension liability into its calculation of fringe benefits.

Missing Elements in the City Calculation: Annual Leave, Employee Allowances, and Overtime

There are certain fringe benefits that seem to be missing from the City's calculation.

The salary data in the City's memo is labeled as "FY09 Salaries," and the salary data is later referred to in other portions of the memo as "budgeted salaries." It is unclear whether the City as part of this salary figure includes overtime. According to the BLS, "Supplemental Pay," which includes overtime, is considered a "benefit."[3]

In Calendar Year 2005, citywide overtime costs exceeded $44 million. The inclusion of overtime costs for the City **will substantially increase the fringe benefit rate**.

Payment for time not worked, such asvacation, holiday, paid breaks, and personal leave is also a fringe benefit and it is customary for fringe benefits to account for "annual leave" as a separate line item. The line item of "Unused Sick Leave" raises a red flag – in that this item contains a relatively small expenditure in relation to overall budgeted salaries. This item does not include vacation and other forms of annual leave.

What is reflected in the calculation provided by the city appears to be only "old unused sick leave" that accrued under an old policy covering employees with sick leave balances prior to 1981. A recent City Auditor examination uncovered abuses in the

Annual Leave
At a Glance

The City of San Diego's policies governing holidays and "annual leave" are as follows:

Holiday Leave:
11 days annually (10 set with 1 floating day)

Annual Leave:
17 days (Service Years 1 – 5)
22 days (Service Years 6 – 15)
27 days (Service Years 16 and up)

[3] Bureau of Labor Statistics. "Employer costs per hour worked for employee compensation and costs as a percent of total compensation: State and local government workers, by major occupational and industry group, September 2008."

accounting and monitoring of the program.[4] Included in that report was a financial accounting of the value of the sick leave, with the audit report noting "based on data provided by the Payroll Division, we found there are 193 current employees with 10,037.1 hours of old sick leave valued at $439,680."

The city may want to reflect the cost of "annual leave" at least in presentation and in calculation if not already included. In Calendar Year 2005, the value of holiday and annual leave was in excess of $80 million. With salary adjustments since that time, this number would likely be higher. Given the generous annual leave package provided to City workers, and taking into account the size of the City's payroll, adding the cost of "annual leave" **will substantially increase the fringe benefit rate.**

Other fringe benefits should also be considered for inclusion in the city's calculation. For example, the city provides various allowances in its labor contracts. These perks include:

- **Transportation allowances** – including mileage reimbursements, auto allowances, and personal use of city vehicles
- **Uniform allowances** – For example, pursuant to the contract with Local 145, each firefighter receives $900 per year for uniform allowance.
  Presidential Leave – wherein the city covers the compensation for the union leaders
- **Tuition reimbursements** – For example, the contract with the Municipal Employees Association (MEA) provides up to $1,000 per employee per year.
  Other items – including dependent care, membership in professional associations, wellness programs, etc.

Illustrative cost figures for these items were not readily available as in the case of holidays and annual leave.

Raising these calculation issues will help refine the city's understanding of its true fringe benefit rate and educate decision-makers and the public on the true cost of benefits provided to city workers.

The City of San Diego may want to include additional items as fringe benefit costs – particularly overtime, annual leave, and any allowances provided city employees pursuant to its labor contracts.

[4] http://www.sandiego.gov/auditor/pdf/tatarcloseout.pdf

City Fringe Benefits Significantly Higher Than National Benchmarks

The City memorandum compared benefits to budgeted salaries to calculate an overall fringe rate. Another common method of computing the proportional value of employee benefits, and the method used by the Bureau of Labor Statistics (BLS) and U.S. Chamber of Commerce, is the computation of "employee compensation and costs as a percent of total compensation."

This method varies from the City's memo, in that all costs associated with employee compensation are included in the denominator. This makes the percentage value representing benefits equal to a percentage of total compensation as opposed to a percentage of salaries. If the City's data were comprehensive (and satisfactorily addressed the concerns above) it would be suitable for a comparison to BLS.

As it stands now, the City's figures restated in the BLS methodology would express fringe benefits at **38% of compensation**. This exceeds the BLS published national average for state and local government of **34.2% of compensation.** If additional adjustments in the treatment of overtime, annual leave, and employee allowances were needed in the city calculation, this would result in an **even higher fringe rate** when using the BLS methodology.

Even if the City's fringe rate were just 38%, reducing the fringe proportion of total compensation to 34% would produce savings of $60,894,264 for the City. The City currently faces a FY 2010 budget deficit of $54 million.

Another way to compare the City of San Diego to BLS benchmarks is to examine state and local government employer costs per hour for employee compensation. Using this metric, the **data shows City employee compensation (salaries and benefits) to be significantly higher than the national average.**

The City FY 2009 budget includes 10,729 budgeted employees. Assuming 40-hour workweeks and 52 weeks in a year, the City's total compensation costs per hour exceed the BLS statistics by almost 15% ($45.08 per hour vs. $39.18 per hour worked.) Keep in mind that accounting for the numerous potential omissions pointed out in the previous section will likely push the City's costs even higher.

Notwithstanding the differences in methodology between the City and BLS, the City may want to compile its fringe data in a manner that allows for a focus on its line item fringe costs. This will improve the City's ability to compare its costs to benchmarks in order to more accurately identify its relative standing.

San Diego Retirement Benefits Higher Than Comparisons

With retirement costs by far the largest portion of fringe benefit costs for the City, a line-item analysis of retirement alone provides a key benchmark. Considerable analysis and benchmarking on the City's retirement benefits has already been conducted – with the determination that the benefits are exceedingly high.

In 2004, the City's Pension Reform Committee similarly determined that "the City's pension benefits are generous by almost any standard applied."

In 2008 the City had Mercer compute the income replacement ratio provided to city employees under the two retirement benefit systems offered by the city.

The analysis of income replacement ratios provided by Mercer reveals that the defined benefit pension plan provides employees with a range of 67.0% - 129.5% of single-highest-year salary. In my experience, this represents an astoundingly high income replacement ratio, especially when taking the Deferred Retirement Option Plan (DROP) into account.

In reference to the DROP program, the current 7.75% guaranteed annual return for DROP program participants is completely out of line with current market interest rates for Treasury Bills. Recently, the average yield for a one-year Treasury bill rose to .54%[5], and as of February 13, 2009, the Long-Term Real Rate Average for

Mercer Analysis: City of San Diego General Members	
Defined Benefit Multiplier	
Age 67	2.80%
Age 65	2.80%
Age 62	2.65%
Age 60	2.55%
Age 55	2.50%
Defined Benefit Cap	90%
Years in Final Average Compensation	1
Defined Benefit Member Rate	10.07%
Defined Benefit Death and Disability Benefits	SDCERS
Defined Contribution City Rate	6.05%
Defined Contribution Member Rate	6.05%
Income Replacement Ratio	
Age at Hire for Illustrative Member	35
Retire at Age 67	
Defined Benefit	89.60%
Defined Contribution	39.90%
TOTAL	129.50%
Retire at Age 65	
Defined Benefit	84.00%
Defined Contribution	35.00%
TOTAL	119.00%
Retire at Age 62	
Defined Benefit	71.60%
Defined Contribution	28.60%
TOTAL	100.20%
Retire at Age 60	
Defined Benefit	63.80%
Defined Contribution	25.00%
TOTAL	88.80%
Retire at Age 55	
Defined Benefit	50.00%
Defined Contribution	17.00%
TOTAL	67.00%
Member Contribution Rates	
Defined Benefit	10.07%
Defined Contribution	6.05%
TOTAL MEMBER	16.12%
City Contribution Rates	
Defined Benefit	10.07%
Defined Contribution	6.05%
TOTAL CITY	16.12%

5 "Short-term T-bill rates rise." *The Boston Globe*. February 10, 2009.

Treasury bills (more than 10 years) reached 2.41% and the Treasury Long-Term Rate (more than 10 years) reached 3.76%.[6]

When the City withdrew from Social Security it established SPSP (for general workers, excluding public safety). As the Mercer analysis demonstrates, the presence of the SPSP retirement plan significantly increases the value and percentage rate of the City's retirement benefits, as employees are able to voluntarily contribute 3.05% of their salary, matched by the City, on top of the required 3% contribution and City match. If a City worker contributes the maximum rate allowed, a total of 12% of their salary would be set aside in a retirement account with half of that (the City's contribution) constituting a fringe benefit. According to the City's data, SPSP cost the City almost $24 million for FY 2009, or 3.70% of compensation. (As in previous examples, this assumes the City's data is comprehensive.)

Some have argued that the city's fringe rate is high, but when adjusted for the lack of Social Security, is in line with national averages. The data does not support this contention.

Reclassifying the percentage of compensation dedicated to Social Security in the BLS data as a retirement benefit instead of a "legally required" benefit shows that on average, state and local governments spend **11.50%** of compensation on retirement benefits. By comparison, the City of San Diego spends double that, **22.35%** of compensation, on retirement benefits. Interestingly, while the validity of including the unfunded pension liability was addressed earlier, removing this from calculations reveals the City of San Diego still exceeds the BLS benchmarks. If the FY 2009 normal cost of $68,610,000 replaces the entire ARC payment provided in the City's memo, San Diego *still* spends a greater proportion of compensation (13.10%) on retirement.

Note that any General Fund expenditures related to "Preservation of Benefits" are not mentioned in the City's memo. ("Preservation of Benefits" are monies paid out of the General Fund because the SDCERS benefits for an individual were so generous that they exceed the legally allowable limits set by the IRS.) Furthermore, the recently announced $2 billion pension liability will exert tremendous upward pressure on the City's ARC payment for FY 2011 – potentially driving this payment above $200 million.

Even after removing the SPSP costs for replacing Social Security, the costs of retirement for San Diego City workers still significantly exceed national benchmarks for state and local government for retirement and Social Security programs.

[6] U.S. Department of the Treasury.

City Health Care Benefits Higher Than Comparisons

Keeping with a line item comparison of fringe benefits, the second largest item pertains to health insurance costs – for both current city workers and retirees. Together health care costs reflect $110 million, or 17.5% of budget salaries using the city's fringe rate calculation.

Using only the data provided by the City in its memo, on a proportional basis, the City of San Diego spends more on health care fringe benefits than the BLS national benchmarks (11.52% vs. 10.8% of total compensation).

Another comparison demonstrates the City of San Diego's higher costs. The Bureau of Labor Statistics offers a helpful benchmark concerning the percentage of the cost of health insurance covered by state and local governments across the country.

> *"Employer share for single coverage was greater in State and local government (90 percent for full time; 88 percent for part time) than in private industry (81 percent). For family coverage, the employer share of premiums was similar for private industry and government, 71 and 73 percent, respectively (both figures for full-time)."* [7]

Applying this benchmark to the City of San Diego reveals that the city is bearing a higher percentage of health insurance costs than counterparts in state and local government.

The city has negotiated various contribution levels for its employees depending on their bargaining unit. Under this "Flexible Benefits Plan" a city employee can use their flat allowance for healthcare, dental, vision, and dependent care.

The following chart provides the allocations. Whatever portion is not used by the employee can be deposited into a 401(k) account or redeemed in the form of a cash payment. Should an employee already have coverage through a spouse, the employee is eligible for cash payout ranging from $1500 for police and fire to $6075 for MEA members.

City Contributions Under "Flexible Benefits Plan"

FY 2008 - 2009 Flexible Benefits Plan					
	City Contributions for City Employee Health Care				
Medical Insurance Coverage	**Police and Fire**	**MEA**	**Local 127**	**DCAA**	**Unclassified**
Waiver	$1,500	$6,075	$5,575	$4,000	$4,500
Employee Only	$4,701	$6,075	$5,575	$7,701	$7,701
Employee + Spouse/Partner	$7,699	$6,075	$5,575	$11,212	$10,699
Employee + Family	$9,294	$6,075	$5,575	$11,579	$12,294

[7] Bureau of Labor Statistics, "Employee Benefits in the United States, March 2008" http://www.bls.gov/news.release/ebs2.nr0.htm

The city offers a variety of health insurance plans, including Kaiser, HEALTHNET HMO, HEALTHNET PPO, and Sharp. For single coverage and family coverage, the most affordable plan was Kaiser at $3,486 and $10,598 respectively.

	Single $3486	Family $10598	Percent Single	Percent Family
Police and Fire	4701	9294	134%	88%
MEA	6075	6075	174%	57%
Local 127	5575	5575	160%	53%
Manager	7701	12294	221%	116%
DCAA	7701	11579	221%	109%

For ***single*** health insurance coverage, comparing costs to the most affordable plan available to City workers, the City of San Diego's coverage of costs across its employee units ranges from a low of **135%** for Police and Fire to a high of **221%** for DCAA and Unclassifieds. According to BLS, the average cost covered by state and local government for individual health insurance coverage is **90%** for single coverage.

Benchmarked against this figure alone, the city of San Diego's contribution to ***single*** employee health insurance coverage can be said to be **significantly higher for all employee units** than the average coverage provided by other state and local government.

For ***family*** health insurance coverage, comparing costs to the most affordable plan available to City workers, the City of San Diego's coverage of costs across its employee units ranges from a low of **53%** for Local 127 to a high of **116%** for Unclassifieds. According to BLS, the average cost covered by state and local government for family health insurance coverage is **73%** for family coverage.

Benchmarked against this figure alone, the city of San Diego's contribution to ***family*** employee health insurance coverage is **lower for some employee units** and **significantly higher for other employee units** than the average coverage provided by other state and local government.

Without knowing participation rates for the family plan for the only two employee units where the coverage percentage is lower than the national average, a total percentage of health care costs in excess of the national average cannot be determined.

In addition, it is important to note that the comparisons above do not include payments made for retiree health liability and to pre-fund the retiree health care cost for current city workers. The city's retiree health care line item is $50 million – with $23.1 million allocated to fund future retiree health care costs for current city workers.

Engaging in Further Analysis and Reform of San Diego Fringe Benefits

The initial calculation you obtained from the city's Office of Financial Management was a good start on what needs to be a more robust discussion on the cost of fringe benefits for your city workers.

I would encourage you to continue to press for dialogue and refined data on fringe benefits. My next step recommendations are:

- Request that either the Office of Financial Management or your Independent Budget Analyst respond to the methodological questions raised in this report.
- Draw out any criticism of the definition of what constitutes "fringe benefits" from the labor unions and seek to respond to their concerns in order to come to a common definition.
- Comparisons of national fringe benefit rates can be useful, but the preferred approach should be to examine your benefit structure in relation to your ability to recruit and retain employees.
- Seek job-function-specific compensation studies – such as the one the city conducted two years ago looking at Police compensation. Job-function comparisons are far more helpful in setting salary and benefits.
- Monitor recruitment and retention metrics for each job function, particularly as you propose and implement changes in salary and benefits. If you reform compensation for a specific job function and it has no impact on recruitment and retention, you may consider additional reforms in that job function in the future. The converse is true: if you reform compensation and start seeing recruitment and retention problems, your city should be ready to react quickly and make adjustments.
- Reduce incentives for early retirements, such as DROP programs or post retirement healthcare subsidies. Today retirees at age 55 have an expected life span of 27 years. Working five more years will cut pension costs in half and retiree health costs even more.
- Stay the course: labor unions will not like the questions you are posing nor appreciate the data sets you are presenting. You pressing these issues only make it harder to do what they are supposed to do: advocate for higher compensation (salaries and benefits) for their members.
- It is my hope that this report contains the kind of initial benchmarks, comparisons, and suggestions for additional inquiries that will allow your city to reform its fringe benefits to more sustainable levels. We stand ready to assist you and your colleagues as they explore these and other fiscal issues.

ATTACHMENTS:
Appendix 1: City of San Diego Fringe Rate Calculation, August 18, 2008
Appendix 2: Bureau of Labor Statistics Data

About Californians for Fiscal Responsibility

Founded in 2007, the California Foundation for Fiscal Responsibility is a 501(c)4 organization committed to educating the public and key decision makers about California public employee retirement benefit issues and developing fiscally responsible solutions that are fair to employees, employers and taxpayers. CFFR believes managing the pension and retiree health care obligations promised to public employees is the most critical public finance issue of this decade.

CFFR will use a variety of forums and techniques to educate the public and decision makers, including seminars, media events, personal meetings, issue research and publications.

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About Marcia Fritz, CPA

Marcia Fritz is a principal in the Sacramento area-based Marcia Fritz & Company, Certified Public Accountants. Ms. Fritz has over 34 years of public accounting experience with an international firms and her own firm. She maintains a direct client relationship for a number of government and nonprofit entities by providing a host of assurance and business consulting services. In addition, Ms. Fritz performs consulting engagements including; strategic planning, economic modeling, review of various forecasts and projections, contract pricing studies, compensation modeling and specialized internal control and agreed upon procedures projects.

In addition to running her own accounting firm, Ms. Fritz is Vice President of California Foundation for Fiscal Responsibility which is advocating for pension reform, post retirement healthcare reform, and governance reform related to benefits granted to state and local government workers.

Ms. Fritz is also advocating for improvements in Generally Accepted Governmental Accounting Standards as they relate to public pensions. As a result of her experience and expertise, The Governmental Accounting Standards Boardappointed her on January 27, 2009 to their Task Force on Postemployment Benefits Accounting and Financial Reporting to consider the possibility of improvements to the existing standards of accounting and financial reporting for postemployment benefits—including pension benefits and other postemployment benefits—by state and local governmental employers.